

IN THE COURT OF APPEALS OF TENNESSEE  
AT KNOXVILLE  
July 23, 2008 Session

**DAVIS ENTERPRISES, LLC v. REAGAN FARR, COMMISSIONER OF  
REVENUE, STATE OF TENNESSEE**

**Appeal from the Chancery Court for Sevier County  
No. 07-2-069 Telford E. Forgety, Jr., Chancellor**

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**No. E2008-00140-COA-R3-CV - FILED NOVEMBER 25, 2008**

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The plaintiff, Davis Enterprises, LLC (“the LLC”), sued the Commissioner of Revenue of the State of Tennessee (“the Commissioner”) challenging the Commissioner’s sales and use tax assessment of \$225,774.87 against the LLC. The trial court determined that an assessment was appropriate but only in the amount of \$564. Following the trial court’s judgment, the LLC sought an award of attorneys’ fees and expenses under the authority of Tenn. Code Ann. § 67-1-1803(d) (Supp. 2007). The trial court held that the Commissioner was the prevailing party and, as a consequence of that ruling, denied the LLC’s application. The LLC appeals. We reverse and remand for further proceedings.

**Tenn. R. App. P. 3 Appeal as of Right; Judgment of the Chancery Court  
Reversed; Case Remanded**

CHARLES D. SUSANO, JR., J., delivered the opinion of the court, in which HERSCHEL P. FRANKS, P.J., and D. MICHAEL SWINEY, J., joined.

Dudley W. Taylor, Knoxville, Tennessee, for the appellant, Davis Enterprises, LLC

Robert E. Cooper, Jr., Attorney General and Reporter, and Brad H. Buchanan, Assistant Attorney General, Office of the Attorney General, Tax Division, Nashville, Tennessee, for the appellee, Reagan Farr, Commissioner of Revenue, State of Tennessee

**OPINION**

**I.**

On July 10, 2004, the Commissioner made a sales and use tax assessment against Charles R. Davis, a sole proprietor doing business as Reliable Printing. According to the Commissioner’s counterclaim, Mr. Davis “was assessed \$163,836.28 in tax, \$40,959.01 in penalties, as well as interest.” In September 2004, the LLC was formed. Shortly after the LLC was formed, Mr. Davis

and his wife, Patricia Lynn Davis, transferred to the LLC several parcels of real property owned by the Davises as tenants by the entirety. On September 27, 2005, this prompted the Commissioner to make an assessment against the LLC in the amount of \$225,774.87. The Commissioner proceeded against the LLC on the authority of the following statutes:

Tenn. Code Ann. § 67-1-1444 (2006)

(a) When assets are conveyed or obligations are created by a person owing taxes to the state, on or after the date any such taxes are incurred, and such conveyance of assets or creation of obligations is in violation of the provisions of title 66, chapter 3, then the commissioner may proceed to collect such tax debt from the transferee, pursuant to the provisions of this part, in the same manner as the commissioner otherwise could have collected such debt from the transferor.

(b) The liability of any such transferee shall be limited to the fair market value of the assets conveyed at the time of the transfer from the original taxpayer or the amount of any such obligation at the time the obligation is created.

Tenn. Code Ann. § 66-3-101 (2004)

Every gift, grant, conveyance of lands, . . . had or made and contrived, of malice, fraud, covin, collusion, or guile, to the intent or purpose to delay, hinder, or defraud creditors of their just and lawful actions, suits, debts, accounts, damages, penalties, forfeitures; . . . , shall be deemed and taken, only as against the person, such person's heirs, successors, executors, administrators, and assigns, whose debts, suits, demands, estates, or interest, by such guileful and covinous practices, shall or might be in any wise disturbed, hindered, delayed, or defrauded, to be clearly and utterly void; any pretense, color, feigned consideration, expressing of use, of any other matter or thing, to the contrary notwithstanding.

The LLC brought suit in the trial court against the Commissioner. It sought to abate the assessment. The Commissioner filed an answer and counterclaim asserting that the real estate transfers to the LLC were fraudulent and that the State was entitled to a judgment against the LLC in the amount of \$225,774.87. The Commissioner did not request that the transfers be set aside.

After a bench trial, the court below held that the transfers of real estate from the Davises to the LLC “were made with the ‘actual intent to hinder, delay, or defraud’ the [Commissioner] as a

creditor, in violation of Tenn. Code Ann. § 66-3-305(a)(1).”<sup>1</sup> (Footnote added.) Having determined that the transfers were fraudulent, the trial court proceeded to the issue of the “fair market value of the assets conveyed at the time of the transfer.” *See* Tenn. Code Ann. § 67-1-1444(b). The court held that “the value of the expectancy of survivorship interest of [Mr.] Davis in the [real property] as of the date of transfer was \$564.” The remainder of the original assessment of \$225,774.87 was abated. As can be seen, the trial court abated 99.75% of the assessment.

The determination as to the “prevailing party” in the litigation was deferred by the trial court pending a possible appeal. Neither party appealed. The LLC then filed its application for “attorneys’ fees and expenses” under Tenn. Code Ann. § 67-1-1803(d). The Commissioner opposed the application. The trial court found that the Commissioner was the prevailing party. Accordingly, it denied the LLC’s application.

## II.

The LLC raises one issue on appeal. Taken verbatim from its brief, the issue is as follows:

Whether the trial court erred in determining that [the LLC] was not the prevailing party, although the [Commissioner’s] assessment was reduced from \$225,774.87 to \$564.

## III.

“The construction of statutes and of regulations promulgated pursuant to statutes and the application of those statutes and regulations to undisputed facts are questions of law.” *Time Warner Entertainment, L.P. v. Chumley*, No. M2005-00291-COA-R3-CV, 2006 WL 1559625, at \*2 (Tenn. Ct. App. M.S. filed May 31, 2006) (citing *Beare Co. v. Tennessee Dept. of Rev.*, 858 S.W.2d 906, 907 (Tenn. 1993)). In the instant case, the parties filed a joint stipulation of undisputed facts. Since the facts are not in dispute, the only issue raised by the LLC presents a pure question of law. Our review is *de novo* with no presumption of correctness attaching to the trial court’s legal judgment. *Taylor v. Fezell*, 158 S.W.3d 352, 357 (Tenn. 2005).

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<sup>1</sup>Tenn. Code Ann. § 66-3-305(a)(1) (2004) provides as follows:

A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor’s claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:

(1) With actual intent to hinder, delay, or defraud any creditor of the debtor; . . .

The primary issue in this case concerns the trial court's construction and application of Tenn. Code Ann. § 67-1-1803(d).<sup>2</sup> That portion of the statute provides as follows:

The court shall award to the prevailing party reasonable attorneys' fees and expenses of litigation up to twenty percent (20%) of the amount assessed or denied, including interest after payment.

In the case of *Carson Creek Vacation Resorts, Inc. v. State*, 865 S.W.2d 1 (Tenn. 1993), the Supreme Court analyzed Tenn. Code Ann. § 67-1-1803(d). *Id.* at 2-3. The Court noted that the most basic rule of statutory construction is to ascertain and give effect to the intention and purpose of the legislature. *Id.* at 2 (citing *Worrall v. Kroger Co.*, 545 S.W.2d 736 (Tenn.1977)). The High Court observed that the legislative intent is best ascertained from the natural and ordinary meaning of the words used, without forcing a construction that would limit or extend the meaning of the words. *Id.* (citing *National Gas Distributors, Inc. v. State*, 804 S.W.2d 66 (Tenn.1991)). The Court in *Carson Creek* concluded that where the language of a statute is plain, clear and unambiguous, "the duty of the courts is simple and obvious, namely, to say *sic lex scripta*, and obey it." *Id.* (quoting *Miller v. Childress*, 21 Tenn. 319, 321-22 (1841)). The rule stated in *Miller* remains as a guide to modern courts on the issue of statutory construction. *Carson Creek*, 865 S.W.2d at 2, (citing *Austin v. Memphis Publishing Company*, 655 S.W.2d 146 (Tenn.1983)). Applying these rules, the Supreme Court in *Carson Creek* found that Tenn. Code Ann. § 67-1-1803(d), "by its ordinary meaning, allows no discretion to the trial court in the award of attorneys' fees and expenses of litigation to the prevailing party in tax litigation." It thus concluded that the award is mandatory. *Carson Creek*, 865 S.W.2d at 2.

#### IV.

In point of time, Mr. Davis and his wife formed the LLC and transferred to it 11 parcels of real estate in the month following the month in which he learned of the assessment against him. *All of the transferred parcels were owned by the Davises as tenants by the entirety.* As previously noted, the subsequent assessment against the LLC was made pursuant to Tenn. Code Ann. § 67-1-1444(a). The Commissioner argued that the assessment against the LLC was appropriate because, according to him, the transfers were fraudulent as to the State. The LLC disputed that the transfers were in violation of title 66, chapter 3, and vigorously contested the issue of fraud.

The trial court decided that Mr. Davis had violated the Uniform Fraudulent Transfer Act, Tenn. Code Ann. §§ 66-3-101 *et seq.* The Commissioner argued in the trial court, and now argues in this court, that he was the prevailing party on the "fraud" issue. He concedes, as obviously he must, that the LLC "was largely successful on the second" issue.

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<sup>2</sup> Although subsection (d) was amended after this lawsuit was filed, the parties appear to be in agreement that the amendment does not have any effect in this case.

The Commissioner relies on the case of *Federated Stores Realty, Inc. v. Huddleston*, 852 S.W.2d 206 (Tenn. 1992). In that case the Supreme Court addressed an issue concerning the award of attorneys' fees and expenses in a tax case, using only one sentence: "Inasmuch as each party has prevailed on one issue there is no award of attorneys' fees or expenses of litigation otherwise awarded under [Tenn. Code Ann.] § 67-1-1803(d)." *Id.* at 215. The Commissioner argues that *Federated Stores Realty* is controlling in this case. If *Federated Stores Realty* is applicable and controlling on the facts before us, neither party is entitled to fees or expenses under Tenn. Code Ann. § 67-1-1803(d).

The Commissioner also relies on the doctrine of unclean hands, saying that Mr. Davis had been guilty of bad faith and "a Court of Equity" should not reward his fraudulent conduct by paying his attorneys' fees and expenses of litigation. It is clear from the Supreme Court's analysis of Tenn. Code Ann. § 67-1-1803(d) in *Carson Creek*, however, that under Tenn. Code Ann. § 67-1-1803(d), the trial court has no discretion as to whether to award fees and expenses to a "prevailing party." *Carson Creek*, 865 S.W.2d at 2. An award of attorneys' fees and expenses is mandatory in such a situation. *Id.* The Supreme Court has said, however, that "[t]he court does . . . have limited discretion in determining the amount of the award mandated by the statute and may award any amount up to 20 percent of the total tax assessed or denied, including interest after payment." *Id.* (citing Tenn. Code Ann. § 67-1-1803(d)).

In denying the LLC's application, the trial court stated as follows:

This matter came before the Court on January 11, 2008, upon [the LLC's] Application for Attorney Fees and Expenses of Litigation. The Application was made pursuant to Tenn. Code Ann. § 67-1-1803 (d). [The LLC] asserted that it was entitled to recovery of attorney fees as a prevailing party since the assessment was reduced by the Court from \$225,774.87 to \$564. The [Commissioner] opposed the Application urging the Court to find that [the LLC] was not the prevailing party. After taking into account the Application, supporting and opposing memorandums, statements of counsel and such other matters as the Court deemed pertinent, it agreed with [the Commissioner] that Plaintiff was not the prevailing party. Accordingly, it is hereby

ORDERED that [the LLC's] Application for Attorney Fees and Expenses of Litigation is denied.

The LLC's argument before this court is simple. The Commissioner made an assessment against the LLC under Tenn. Code Ann. § 67-1-1444 in the amount of \$225,774.87. The trial court reduced this assessment to \$564. Under Tenn. Code Ann. § 67-1-1803 (d), the prevailing party is entitled to attorneys' fee and expenses. The LLC argues that since the trial court abated 99.75% of

the assessment, the LLC was the prevailing party and should be awarded its attorneys' fees and expenses of litigation.

As the Supreme Court has suggested in *Nutritional Support Serv., Ltd. v. Taylor*, 803 S.W.2d 213 (Tenn. 1991), there are “degrees of success” in some tax litigation. *Id.* at 217. In *Nutritional Support*, the Commissioner of Revenue argued “that the amount involved and the result obtained are inappropriate in tax cases, because the desired result, winning the case is the prerequisite for receiving any fee; that in tax cases there are no *degrees* of success as in other cases.” *Id.* The Supreme Court explicitly disagreed with this position, saying:

We do not agree with the Commissioner's argument that the amount involved is not a proper consideration, and although in most tax cases the parties win or lose 100% of each issue, *we think there may well be cases in which there are degrees of success*. It would be contrary to the entire history and precedent of litigation to say that in awarding a reasonable fee, the amount at risk should not be a factor in the amount of the fee. No one would seriously contend that, all other factors being equal, the same fee should be awarded in a lawsuit involving \$500,000 that would be a reasonable fee in a case involving only \$50,000.

*Id.* (emphasis added).

Relying on *Nutritional Support*, we have no problem holding that the LLC prevailed in that part of the case concerning the value of Mr. Davis’ interest in the assets he and his wife transferred to the LLC. That holding does not end our inquiry, however. The question remains: Which of the parties “prevail[ed]” in this case under the applicable statute?

In *Federated Stores Realty*, a case in which there were two issues and each party prevailed on one of them, the Supreme Court awarded no attorneys’ fees and expenses under Tenn. Code Ann. § 67-1-1803(d). Although cases actually construing Section 67-1-1803(d) are few in number, this court regularly deals with the concept of the prevailing party in differing contexts. For example, in a recent construction lawsuit, *M. R. Stokes Co., Inc. v. Shular*, No. M2006-02659-COA-R3-CV, 2008 WL 544665, at \*12 (Tenn. Ct. App. M.S., filed February 26, 2008), in considering whether to award costs and expenses to the prevailing party, this Court held that the contractor prevailed on two issues and the owner prevailed on two issues. We concluded, “It would, therefore, be inequitable to say that either party is ‘prevailing.’ ” *Id.*

In its reply brief, the LLC attempts to distinguish *Federated Stores Realty* by arguing that this case does “not involve two separate and distinct issues.” The LLC states, “In this case, a single

issue was presented to the Trial Court. That issue was whether [the Commissioner] was correct in assessing a tax liability against [the LLC] in the amount of \$225,774.87.” We agree that the issue as stated by the LLC is the real issue to be resolved in determining whether there is a “prevailing” party in this case.

The Commissioner makes much of the fact that the subject transfers of real property were fraudulent in nature. He argues that the LLC should not be “rewarded” for its fraudulent conduct by an award of fees and expenses. This argument misses the point. The issue under Tenn. Code Ann. § 67-1-1803(d) is not what kind of conduct *prompted* the litigation; the concept of “prevailing party,” as a practical matter, addresses itself to who *won* the litigation. While the Commissioner won the “battle” of the fraud issue, his victory was a hollow one, a judgment of \$564 – hardly a successful litigation effort.

The Commissioner’s assessment and its counterclaim were founded on his assertion that the LLC owed the State \$225,774.87. This case was about money, pure and simple. How much did the LLC owe the State? Since the properties transferred to the LLC were owned by the *sole* taxpayer, Mr. Davis *and* his wife as tenants by the entirety, the only value that the State could assess and hope to collect was the value of Mr. Davis’s expectancy – the expectancy that he would outlive his co-tenant, his wife. That interest was valued by the trial court at a paltry \$564. That amount is .2498063% of the amount claimed and sought by the Commissioner. The LLC “won” this lawsuit. By any reasonable evaluation, it is the prevailing party.

V.

The judgment of the trial court is reversed. This case is remanded to the trial court for the purpose of holding a hearing to set the LLC’s “reasonable attorneys’ fees and expenses” pursuant to Tenn. Code Ann. § 67-1-1803(d). Costs on appeal are taxed to the appellee Reagan Farr, Commissioner of Revenue, State of Tennessee, or his successor in office.

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CHARLES D. SUSANO, JR., JUDGE